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No. 879

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In the Supreme Court of the United States

OCTOBER TERM, 1961

F. P. BAUGH, INC., a California corporation,
Petitioner,

vs.

LITTLE LAKE LUMBER COMPANY, a.k.a. LITTLE LAKE LUMBER CO., a partnership; UNITED STATES OF AMERICA, et al.,
Respondents.

Brief of California Bankers Association, *Amicus Curiae*, in Support of Petitioner's Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit.

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By consent of petitioner, F. P. Baugh, Inc., and of respondent, United States of America, filed herewith, California Bankers Association files this brief as *amicus curiae*.

STATEMENT OF INTEREST OF THE AMICUS CURIAE

The *amicus curiae*, California Bankers Association, is a nonprofit corporation, the membership of which includes most of the commercial banks and trust companies active

in the State of California. Loans made by banks and trust companies to partnerships often are secured by mortgages upon partnership property. Accordingly, questions of law affecting the validity and priority of liens created by present and future mortgages are of vital concern to these lending institutions.

SUMMARY OF REASONS FOR GRANTING PETITION

1. The decision of the Court of Appeals that the Notice of Federal Tax Lien filed against an individual partner was sufficient to create a lien prior in time and superior in right to a mortgagee's lien on specific partnership assets is in conflict with decisions of this Court and of two Courts of Appeals which hold that a federal tax lien filed only against an individual partner does not attach to specific partnership assets.

2. The decision of the Court of Appeals is also in conflict with the long-established rule, enunciated and followed by this Court and various Courts of Appeals, that state law controls the question of whether one against whom a federal tax lien is filed has any "property or rights to property" subject to the lien.

3. The decision of the Court of Appeals raises an important question regarding administration of the federal tax statutes and creates confusion requiring clarification and resolution by this Court.

REASONS FOR GRANTING PETITION

1. The Court of Appeals in the instant case held that a Notice of Federal Tax Lien which merely named one of the partners in a partnership did not properly name the partnership itself so as to create a lien upon all of the partnership's assets superior to the rights of the partner

ship creditors. However, the Court of Appeals went on to hold that the naming of the individual partner in a Notice of Federal Tax Lien was sufficient to give rise to a lien upon a portion of the partnership assets superior to the rights of partnership creditors.

This holding that the creation of a valid federal tax lien upon the "property and rights to property" of an individual general partner of a limited partnership by itself establishes a lien against a portion of the partnership assets valid against a subsequent mortgagee for value of such partnership property, is directly in conflict with the decision of this Court in *United States v. Kaufman*, 267 U.S. 408 (1925) and with the decisions in *United States v. Worden*, 213 F.2d 509 (6th Cir. 1954), and *Adler v. Nicholas*, 166 F.2d 674 (10th Cir. 1948). Although the Court of Appeals attempts to distinguish this line of cases on the basis that the tax obligation in the instant case was a partnership obligation, its prior holding that the Notice of Federal Tax Lien was not effective against the partnership reduces this alleged point of distinguishment to a "distinction without a difference".

2. Further, the failure of the Court of Appeals to determine whether applicable law gave the individual against whom the lien was asserted any "property or rights to property" in specific partnership assets is contrary to principles enunciated by this Court in *Aquilino v. United States*, 363 U.S. 509 (1960); *United States v. Durham Lumber Co.*, 363 U.S. 522 (1960); and *United States v. Bess*, 357 U.S. 51 (1958). These decisions make clear that the statutes in question (26 U.S.C. 6321 and 6322) create no property rights, but merely attach consequences, federally defined, to rights created under *state law*. Aside from the instant case, the principles of these decisions have been uniformly

applied by the Courts of Appeals. *Allan v. Diamond T Motor Car Company*, 291 F.2d 115, 116 (10th Cir. 1961); *Central Surety & Insurance Corp. v. Martin Infante Co.*, 272 F.2d 231, 233 (3d Cir. 1959); and *Fidelity & Deposit Co. v. New York City Housing Authority*, 241 F.2d 142, 144 (2d Cir. 1957). Since the instant decision presently stands in conflict with the principles expressed and followed in these cases, the perpetuation of this holding would raise inconsistencies in administration of federal tax laws among the circuits. It frequently has been stated that such inconsistencies are to be avoided, *e.g.*, see *Aquilino v. United States*, *supra*, at 363 U.S. 514.

As noted above, the Court of Appeals did not consider whether McCulloch, the partner against whom the Notice of Federal Tax Lien was filed, had any "property or rights to property" in the partnership assets. If it had followed this approved procedure, however, it would have found that under well settled rules of both California partnership law and limited partnership law, a general partner has no right to possession of specific partnership assets for other than partnership purposes.

See,

California Corporation Code Secs. 15024-28, 15509; *Sherwood v. Jackson*, 121 Cal. App. 354, 8 P.2d 943 (1932).

See also,

Baum v. Baum, 51 C.2d 610, 612-13, 335 P.2d 481, 483 (1959).

Accordingly, it appears clear that under the applicable California law, the individual partner in this case had no property rights in the specific partnership assets. Since the power of the federal taxing authority never extends beyond the rights of the taxpayer upon whom levy is

sought (*Stuart v. Willis*, 244 F.2d 925, 929 (9th Cir. 1957)), it must follow that the partnership assets should not be held directly subject to the federal tax lien filed against the individual partnership in this case.

This analysis is true not only in California, but also in the forty states that have adopted the Uniform Partnership Act (1 *Rowley on Partnership* Section 33.2 (2d ed. 1960)). In fact, it appears that one of the main purposes of the drafters of the Uniform Partnership Act was to provide that partnership property could not be made subject to attachment or execution on the debt of an individual partner. (See, Commissioner's Note to Section 25 of the Uniform Partnership Act in 7 Uniform Laws Annotated 144, 50.) The effect of the Court of Appeals' decision in this case is to sweep away the distinctions between the rights of an individual partner's creditors and partnership creditors as fixed in the Uniform Partnership Act and to allow a partnership creditor to be subordinated to the interest of a creditor of an individual partner.

3. The decision of the Court of Appeals raises a question of general importance in the administration of the federal tax laws requiring clarification by this Court. As might be expected, creditors in states in which the Uniform Partnership Act has been adopted have relied on what have been considered to be well settled rules regarding the priority of partnership creditors and individual partner's creditors discussed above. By searching public records to determine whether a loan secured by partnership assets should, or can, be made, or whether a further optional advance on a loan so secured should, or can, be made, it has been necessary to search under the partnership name only. The effect of this decision of the Court of Appeals not only places in jeopardy numerous loans secured by

partnership assets that already have been made, but until the question of the reach of federal tax liens filed against an individual partner has been resolved by this Court, creditors must determine, at their peril, the identity of all partners in the partnership in question and search each partner's name. Needless to say, the burden of conducting this search will, especially in the light of the wide-spread use of multi-party partnerships in real estate development, be extremely onerous, time consuming and, because of delay in processing secured transactions, a hindrance to those carrying on business in a partnership form. Even more disconcerting, however, is the difficulty faced by a creditor attempting to determine the composition of a partnership in order to obtain the proper names for search. For example, there is no public record of the membership of general partnerships in California, and creditors must now act at their peril in obtaining this information when making loans. The decision of the Court of Appeals, accordingly, may well give rise to creation of practically unascertainable or "secret" liens upon partnership assets.

On the other hand, under generally accepted principles, the Government is presented with no difficulty in situations in which it has a claim against a partnership. As the Court of Appeals recognized, all that is necessary is that it execute and file a proper Notice of Federal Tax Lien naming the partnership. The result of the decision of the Court of Appeals is to enforce the Government's right to revenue in spite of what well may have been misleading error by the Government, and at the expense of reasonable and prudent commercial practices.

CONCLUSION

For the foregoing reasons, we respectfully submit that the petition for writ of certiorari should be granted.

Dated: May 8, 1962

Respectfully submitted,

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